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Nos. 40, 41, 42

In the Supreme Court of the United States

OCTOBER TERM, 1942

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

THE OHIO LEATHER COMPANY

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

THE STRONG MANUFACTURING COMPANY

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

WARREN TOOL CORPORATION

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

PETITIONER'S SUPPLEMENTAL MEMORANDUM

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At the oral argument petitioner was requested to file a memorandum stating petitioner's position

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with respect to the application of section 43 of the Revenue Act of 1936 to the problem presented here.

The contention is made at pages 18–21 of the Brief for Respondent in No. 40, *Helvering* v. *Ohio Leather Company*, and at page 21 of the Brief for Respondent in No. 42, *Helvering* v. *Warren Tool Corporation*, that because these taxpayers were on the accrual basis of accounting they were, by virtue of section 43, entitled to the credit contained in section 26 (c) (2). This contention is without merit, because principles of accrual accounting have no bearing on the question of whether or not a contract requires a payment or an irrevocable setting aside within the taxable year.

The question here is not whether the taxpayers made payment within the taxable year. They did in fact do so though their contracts did not require it. However, if this were the question section 43 and the principles of accrual accounting might have some application, since a taxpayer on the accrual basis is permitted to treat payments required but not made, or receivable but not received, as having been actually made or received.

Here, however, the sole dispute is whether certain contracts required the taxpayers to pay or set aside irrevocably within the taxable year. The principles of accrual accounting do not affect the meaning of contractual provisions; the effect of

accrual principles is to regard as having been paid that which contracts require to be paid, and accrual principles cannot be applied until the meaning and effect of contractual requirements are ascertained. As the question here is what the taxpayers' contracts required, the question here is one which must be decided in advance of any possible application of accrual principles.

Possibly the effect of the taxpayers' contracts was to cause them to accrue the annual payments as an obligation of the taxable year. The statute, however, allows no credit where a contract merely requires an accrual for or within the taxable year. The contract must require a portion of the earnings or profits of the taxable year "to be paid within the taxable year in discharge of a debt, or to be irrevocably set aside within the taxable year for the discharge of a debt," and no serious suggestion can be made that an accrual is an irrevocable setting aside or a payment.

The taxpayers' contention that section 43 has pertinence is based on the fact that section 43 states specifically that it is to be disregarded in computing the credit provided by section 27 and makes no such statement regarding section 26. The logic of this argument is fully met if any provision of section 26 exists to which accrual principles can be applied. Subdivisions (a) and (b) of section 26 respectively provide credits for "The amount received as interest upon obligations of the United States" and for "85 per centum of

the amount received as dividends." In the determination of credits under these two provisions accrual principles can properly be given effect, so the logic of taxpayers' argument seems to compel a recognition that Congress intended section 43 to be given effect in computing such credits. It does not, however, mean that Congress thought that accrual principles could be applied in determining the effect of every requirement in each subdivision of section 26. Thus, some of the requirements which must be met before a credit under section 26 (c) (2) can be allowed are that a contract exist which be (a) written, and (b) entered into before May 1, 1936. Of course section 43 cannot have pertinence in a consideration of these requirements. Neither can it in a consideration of the year in which such a contract requires payments to be made or irrevocably set aside.

CONCLUSION

The taxpayers' contention that section 43 is pertinent in this case is erroneous. As the other contentions made by the taxpayers are erroneous for the reasons stated in petitioner's brief and at the oral argument, the judgments below should be reversed.

Respectfully submitted.

CHARLES FAHY,
Solicitor General.

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